

SECTION XI

NONCOMPLIANCE

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Briefly, a state agency performs a desk audit, conducts a site visit, or reviews the owner's tenant files and provides the owner with a summary report of its findings. The owner is expected to respond to the state agency within a maximum of 90 days to provide clarification or document that the issues of noncompliance have been addressed. The state agency determines whether the owner clarified that they were always in compliance, has corrected the noncompliance, or remains out of compliance. If the agency determines that either the owner remedied the issue of noncompliance or remains out of compliance, then a Form 8823 must be filed with the Internal Revenue Service. The IRS then sends notification letters, identifying the type of noncompliance reported on Form 8823, to taxpayers with instructions to contact the state agency to resolve the issue. Once the issue is resolved, a "back in compliance" Form 8823 should be filed. A copy of the form IRS 8823 (Report of Noncompliance) is included in [Appendix I](#).

Non compliance is defined as a period of time a development, specific building, or unit is ineligible for tax credit because of failure to satisfy LIHTC Program requirements.

Part 1100 :: Types of Noncompliance

Generally, during the Compliance Period a project is out of compliance and recapture may apply if:

- A. A building or an ownership interest in a building is disposed of (see [Part 1190](#)); or
- B. There has been a change in the applicable fraction or eligible basis that results in a decrease in the qualified basis of the building from one year to the next; or
- C. The building no longer meets the minimum set-aside requirements of Section 42(g)(1), the gross rent requirements of Section 42(g)(2), or the other requirements for the units that are set-aside;
- D. Failure to submit the annual utility allowance documentation, owner certification, tenant income and rent report, or compliance monitoring fees, along with any applicable supporting documentation in a timely manner;
- E. A federal grant is obtained that results in a decrease in basis (see 26CFR 1.42-16, which is included in [Appendix G](#)); or
- F. Failure to properly document the eligibility of tenants to reside in LIHTC units.

Part 1110 :: Consequences

If the project is out of compliance, a penalty could apply to all units in the project (IRS Form 8611). Penalties include:

- A. Recapture of the accelerated portion of the tax credit for prior years;
- B. Disallowance of the credit for the entire year in which the noncompliance occurs;
- C. Assessment of interest for the recapture year and previous years;
- D. Notification to IRS;
- E. Negative pointes on any subsequent LIHTC reservation applications (poor previous participation on the part of the sponsor or the management agent). This will be in effect for a time period of one year or more;
- F. Rejection of future applications. Proposals submitted from sponsors that currently have projects that are out of compliance will not be accepted until the noncompliance is corrected;
- G. Repayment of rent overages; and/or
- H. *De Minimis Errors*. On August 10, 1993, Congress passed the Omnibus Reconciliation Act of 1993 that includes a provision for de minimis errors. Certain de minimis errors may be exempt from noncompliance or recapture as determined by the Secretary of the Department of Treasury.

A copy of form IRS 8611 (Recapture of Low-Income Housing Credit) is included in **Appendix I**.

Part 1120 :: Notification of Noncompliance to Owner

MSHDA is required to provide written notice of noncompliance to the owner if:

- A. Any required submissions are not received by the due dates;
- B. Tenant income certifications, supporting documentation, and rent records are not submitted when requested by MSHDA; and
- C. The project is found to be out of compliance through inspection, review, and/or other means within the provisions of Section 42 of the IRC.

Should any of the submissions required herein, including the Owner Certification, the Tenant Income/Rent Report, or income certifications, supporting documentation, and rent records, not be submitted in a timely fashion, or should there be omissions, MSHDA shall, within 45 working days, notify the owner in writing, requesting such information. The owner will have 20 working days in which to provide the information, after which MSHDA shall notify the Internal Revenue Service of the owner's failure to provide the required information.

Part 1130 :: Notification by Owner to MSHDA

If the management company becomes aware of any noncompliance with the LITHC program requirements, the Low Income Housing Tax Credit Compliance Monitoring staff must be notified immediately.

Part 1140 :: Correction Period

Should MSHDA discover, as a result of an inspection or review, or in any other manner, that the project is not in compliance with Section 42, or that credit has been claimed or will be claimed for units which are ineligible, MSHDA shall notify the owner within 45 working days. The owner will have 20 working days in which to commence appropriate action to cure such noncompliance.

The owner shall have a maximum of 90 days from the date of notice to the owner to cure the noncompliance. In extraordinary circumstances, and only if MSHDA determines that there is good cause, an extension of up to six months to complete a cure for noncompliance may be granted.

Part 1150 :: Reporting Noncompliance to Internal Revenue Service

Actual noncompliance will occur if the potential noncompliance is not corrected within a “reasonable” time period. The term “reasonable” is not defined, and will be applied by the IRS on a case-by-case basis. Potential noncompliance of which the owner or management agent becomes aware must be reported to the state agency, who will in turn report it to the IRS. The IRS ultimately determines whether or not there is noncompliance.

MSHDA is required to file IRS Form 8823, “Low Income Housing Credit Agencies Report of Non-Compliance”, with the IRS no later than 45 days after the end of the correction period (as described above, including extensions) and no earlier than the end of the correction period, whether or not the noncompliance or failure to certify is corrected. MSHDA must explain on IRS Form 8823 the nature of the noncompliance or failure to certify and indicate whether the owner has corrected the noncompliance or failure to certify.

If a building is entirely out of compliance and will not be in compliance at any time in the future, MSHDA will report it on a IRS Form 8823 one time and need not file IRS Form 8823 in subsequent years to report that building’s noncompliance.

A copy of form IRS 8823 (Report of Noncompliance or Building Disposition) is included in **Appendix I**.

Part 1160 :: Recapture

Recapture is defined as an increase in the owner’s tax liability because of a loss in tax credits due to noncompliance with program requirements.

The IRS will make the determination as to whether or not the owner faces recapture of tax credits as a result of noncompliance.

IRS Form 8611 is used by taxpayers who must recapture tax credits previously claimed. A copy of IRS Form 8611 must be sent to the IRS and MSHDA upon completion by the owner. A copy of form IRS 8611 (Recapture of Low-Income Housing Credit) is included in **Appendix I**.

Part 1170 :: Retention of Noncompliance Records By MSHDA

MSHDA will retain records of noncompliance or failure to certify for six years beyond MSHDA's filing of the respective IRS Form 8823. In all other cases, MSHDA will retain the certifications and records described in paragraph (c) of Reg. 1.42-5 for three years from the end of the calendar year MSHDA receives the certifications and records.

Part 1180 :: Liability

Compliance with the requirements of Section 42 is the responsibility of the owner of the building for which the credit is allowable. MSHDA's obligation to monitor for compliance within the requirements of Section 42 does not make the Agency liable for an owner's noncompliance (Reg. 1.42-5(g)).

Part 1190 :: Sale, Transfer, or Disposition of the Project after the Placed-in-Service Date

Generally, any change in ownership of a building or a partnership interest is considered to be a potential recapture event. The owner faces recapture of the accelerated portion of any tax credits claimed on the project. The amount of the repayment is equivalent to approximately 1/3 of the credits claimed on the project. Recapture can possibly be avoided in the owner selling the building or the partnership interest posts a bond satisfactory to the IRS, and the IRS determines that the project is expected to remain in compliance for the balance of the Compliance Period. The new owner of a project could then be eligible to continue claiming tax credits.

When a sale occurs, the owner must submit the following to MSHDA:

- A. An executed copy of the purchase agreement;
- B. Recorded Statutory Warranty Deed indicating ownership or a copy of the title policy indication ownership;
- C. A copy of the bond posted for the project and the completed IRS for 8693, Low Income Housing Credit Disposition Bond, if applicable;
- D. A copy of the IRS 8611, Recapture of Low-Income Housing Credit;
- E. A letter from the previous owner indicating the name, address, and phone number of the new owner;
- F. A letter from new owner indicating name, address, and phone number of the management agent; and
- G. Any other reasonable evidence that MSHDA may deem necessary.

MSHDA will recognize a new owner or ownership entity only after all the required documentation has been submitted. Until such time, all compliance requirements will be the responsibility of the owner of record and any compliance violations will be reported to the IRS under the name of the owner of record.

The IRS has also suggested in Reg. 1.42-5 that, if a building is sold or otherwise transferred by the owner, the transferee should obtain from the transferor all information related to the first year of the credit period so the transferee can substantiate credits claimed.

This section of the compliance manual is intended only to provide a brief, generalized description of the requirements for selling or withdrawing LIHTC projects. The owner should consult an attorney or other professional knowledgeable about the LIHTC program for advice and guidance concerning sales.

Forms pertinent to selling or disposing of LIHTC projects are IRS Form 8611 (Recapture of Low-Income Housing Credit) and IRS Form 8693 (Low Income Housing Tax Credit Disposition Bond), which are included in [Appendix I](#) of this manual. Also, see IRS Revenue Ruling 90-60 (Recapture Bonds) and IRS Revenue Procedures 99-11 (Alternative to Posting a Surety Bond) which are discussed in [Appendix H](#).